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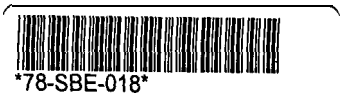

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeals of)
)
DELTA INVESTMENT CO., INC., AND)
DELTA INVESTMENT RESEARCH CORP.)

For Appellants: Brice A. Sullivan
Counsel

For Respondent: Bruce W. Walker
Chief Counsel

David M. Hinman
Counsel

O P I N I O N

These appeals are made pursuant to section 25667 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protests of Delta Investment Co., Inc., and Delta Investment Research Corp., against proposed assessments of additional franchise tax in the amounts and for the years as follows:

with the purpose for the classification, the California courts have held that a financial corporation is one which deals in moneyed capital, as opposed to other commodities, in substantial competition with national banks. (Marble Mortgage Co. v. Franchise Tax Board, 241 Cal. App. 2d 26 [50 Cal. Rptr. 345] (1966); The Morris Plan Co. v. Johnson, 37 Cal. App. 2d 621 [100 P.2d 493] (1940).) Thus, our task with respect to the instant appeal is to determine whether the appellants were dealing in moneyed capital, as opposed to other commodities, in substantial competition with national banks.

For purposes of ascertaining whether a corporation is dealing in moneyed capital in substantial competition with national banks, the courts and this board have focused on the following factors: (1) whether the corporation employs its moneyed capital in financial activities generally engaged in by national banks (The Morris Plan Co. v. Johnson, supra, 37 Cal. App. 2d at 624; Appeals of Croddy Corp., Cal. St. Bd. of Equal., Sept. 1, 1966); (2) whether the combined capital and surplus of the corporation is of an amount comparable to that of national banks (The Morris Plan Co. v. Johnson, supra; Appeal of First Investment Service Co., Cal. St. Bd. of Equal., July 31, 1973); (3) whether the moneyed capital employed in financial activities by the corporation represents a significant portion of its combined capital and surplus (Marble Mortgage Co. v. Franchise Tax Board, supra; Appeal of Winter Mortgage Co., Cal. St. Bd. of Equal., Feb. 5, 1963); (4) whether, if the corporation is engaged in lending activity, the loans are significant in number and amount (The Morris Plan Co. v. Johnson, supra; Appeals of Sterling Finance Corp. Of California, Cal. St. Bd. of Equal., March 25, 1968); and (5) whether the corporation is earning substantial income from its financial activities (Marble Mortgage Co. v. Franchise Tax Board, supra; Appeals of Croddy Corp., supra).

With this background in mind, we turn to the facts presented by the instant appeal. At the outset, however, we observe that the record on appeal contains no information concerning the capitalization of appellants during the years in question, and very little information regarding the nature and extent of their business activities.. In this connection, we note that the burden rests with appellants to prove respondent improperly classified them as financial corporations. (Appeals of The Diners' Club, Inc., Cal. St. Bd. of Equal., Sept. 1, 1967.)

least 64 percent of its total annual income. Finally, the tables indicate that the notes receivable accounts of DIC and DIR increased an average of over $800,000 per year during the period from March 31, 1970 through March 31, 1973, and that the notes receivable account of DIR increased by over $500,000 during its taxable year ended March 31, 1974. While the record does not set forth the precise number and amounts of the loans made by appellants, it is clear that the appellants employed substantial amounts of moneyed capital in connection with their lending activities. Thus, we are convinced that the appellants were dealing in moneyed capital in substantial competition with national banks during each of the taxable years ended March 31, 1971 through March 31, 1974. (See Marble Mortgage Co. v. Franchise Tax Board, supra, 241 Cal. App. 2d at 41; Appeals of Sterling Finance Corp. of California, supra; Appeals of Ponticopoulos, Inc., Cal. St. Bd. of Equal., Sept. 1, 1966.)

The appellants contend that they were not financial corporations during any of the taxable years in question because their financial activities did not constitute the major aspect of their business operations. However, we have previously held that a corporation may be properly classified as a financial corporation even though its financial activities do not constitute all, or even a major part, of its business operations. (Appeals of Croddy Corp., supra; Appeal of Continental Securities Co., Cal. St. Bd. of Equal., Feb. 3, 1944.) The critical question in such cases is not whether the corporation is primarily engaged in financial activities but whether its financial activities bring it into substantial competition with national banks. It would be discriminatory to allow corporations engaged in financial activities in substantial competition with national banks to pay taxes at a lower rate than the national banks on profits obtained from such activities. (See Marble Mortgage Co. v. Franchise Tax Board, supra, 241 Cal. App. 2d at 42.)

The appellants also assert that their lending activities did not bring them into substantial competition with national banks because: (1) they did not offer or advertise their lending services to the public; (2) the loans were made primarily to affiliated companies; and (3) the loans were necessary due to the unavailability of national bank financing.

The facts that the appellants did not offer their lending services to the public and that the loans

taxable year ended March 31, 1975 is erroneously based on the financial activities of DIC during the prior income year.

Generally, a determination by respondent is presumed to be correct and the taxpayer has the burden of proving the determination erroneous. (Todd v. McColgan, 89 Cal. App. 2d 509 [201 P.2d 4141 (1949); Appeal of Robert L. Webber, Cal. St. Bd. of Equal., Oct. 6, 1975.) However, where it is evident that respondent's determination is arbitrary or capricious the presumption no longer avails. (Helvering v. Taylor, 293 U.S. 507, 514 [79 L. Ed. 6231 (1935); Appeal of Morris M. and Joyce E. Cohen, Cal. St: Bd. of Equal., Feb. 19, 1974.)

As we have indicated, respondent's determination that DIC was a financial corporation for the taxable year in question is based solely on the financial activities of DIC during the prior income year. Thus, the assessment for DIC's taxable year ended March 31, 1975 is attributable to respondent's erroneous view of the law and has no factual support in the record. Under the circumstances, we can only conclude that respondent's action in this regard was arbitrary and must be reversed. (See United States v. Hover, 268 F.2d 657, 665 (9th Cir. 1959)

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
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DELTA INVESTMENT CO., INC., AND)
DELTA INVESTMENT RESEARCH CORP.)

ORDER DENYING PETITION FOR REHEARING,

Upon consideration of the petition filed May 8, 1978 by the Franchise Tax Board for rehearing of the Appeal of Delta Investment Co., Inc., we are of the opinion that none of the grounds set forth in the petition constitute cause for the granting thereof and, accordingly, it is hereby ordered that the petition be and the same is hereby denied and that our order of April 6, 1978 be and the same is hereby affirmed.

Done at Sacramento, California, this 27th day of September 1978, by the State Board of Equalization.

_____, Chairman

_____, Member

_____, Member

_____, Member

_____, Member